



INDUSTRY CIRCULAR

DEPARTMENT OF
THE TREASURY

Bureau of Alcohol, Tobacco and Firearms
Washington, D. C. 20226

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DISTILLED SPIRITS TAX INCREASE AND RESULTING FLOOR STOCKS TAX

Proprietors of Distilled Spirits Plants, Importers,
Wholesalers, Retailers, and Others Concerned:

Purpose. This Industry Circular is issued to advise proprietors of an increase in the distilled spirits tax rate, effective October 1, 1985, and of a resulting one-time floor stocks tax. In addition, this circular will describe the procedures for establishing the inventory of distilled spirits to determine the total liability of the floor stocks tax.

Background. The Deficit Reduction Act of 1984 (Public Law 98-369), enacted on July 18, 1984, increased the rate of tax on distilled spirits from \$10.50 to \$12.50 per proof gallon, effective October 1, 1985. All distilled spirits removed from bonded premises on or after the effective date will be subject to the increased tax rate. As a transition to the new tax rate, this Act imposes a one-time floor stocks tax equal to the difference between the old and new tax rates (\$2.00 per proof gallon) on all taxpaid distilled spirits held for sale on October 1, 1985.

Terms Defined. Certain terms used in this circular may need defining to alleviate any confusion. The following definitions should assist concerned proprietors:

Wine gallon. A standard U.S. volumetric gallon.

Proof. The alcohol content of a liquid, stated as twice the percent of alcohol by volume. For example, whiskey with an alcohol content of 40 percent is 80 proof.

Proof gallon. A standard U.S. gallon at 100 proof, or its alcoholic equivalent. For example, 1 gallon of 200 proof spirits would equal 2 proof gallons; 10 gallons of 80 proof spirits would equal 8 proof gallons.

Dealer. Unless otherwise specified, this term includes importers, wholesalers, and retailers of distilled spirits. Also included are taxpaid storage rooms operated by proprietors of distilled spirits plants.

Small or medium-sized dealer. Any dealer whose aggregate gross sales receipts for all products (not just distilled spirits products) for the most recent taxable year ending before October 1, 1985, do not exceed \$500,000.

Controlled group. Any group of incorporated or nonincorporated dealers that have common ownership interests (including States or political subdivisions of States). Generally, a proprietor is considered to be part of a controlled group if at least 50 percent of the company is either owned by, or in common with, another company (or companies).

Open stock. All stock that is not in full cases. Includes both opened and unopened bottles of various sizes, proofs, and brands, whether in storerooms, on the shelf, or behind a bar.

Floor Stocks Tax Liability. The distilled spirits floor stocks tax is imposed on all federally taxpaid or tax-determined distilled spirits that are held for sale on the first moment of October 1, 1985. Dealers of distilled spirits who have 500 wine gallons or less on hand on October 1, 1985, are exempt from the floor stocks tax, although they must file a tax return. All dealers who have more than 500 wine gallons on hand are allowed as a credit against the floor stocks tax an amount equal to \$800 or the amount of tax liability, whichever is smaller. Controlled groups must apply the 500 wine gallon exemption and the \$800 credit to the group as a whole. Proprietors are liable for the floor stocks tax irrespective of the location where their distilled spirits are held. Taxpaid distilled spirits held for sale on Federal property (military installations, Indian reservations, etc.) are not excluded from the tax.

General Inventory Provisions. Liability for the floor stocks tax must be established either by a physical inventory or a record (book) inventory supported by the appropriate source records. The inventory will be the basis for establishing the quantity of distilled spirits held subject to the floor stocks tax as of the first moment of October 1, 1985.

Proprietors who prefer not to take a physical inventory on October 1, may take it anytime between September 23, and October 6, 1985. (Or, if the business is closed before September 23, and will remain closed through October 1, the inventory may be taken on the last business day before closing.) If the physical inventory is not taken between the end of the last business day of September, and the beginning of the first business day of October, it must be reconciled to October 1, 1985. This reconciliation must be supported by records of all receipts and dispositions between October 1, and the date of the inventory.

A record inventory must indicate the exact on-hand quantity of distilled spirits in stock on October 1, and be supported by source records that indicate receipts and dispositions of

distilled spirits. The records of receipt and disposition (such as invoices) must include (1) the name and address of the consignor and consignee, (2) date of receipt and disposition, (3) brand name, (4) kind of spirits, and (5) quantity of spirits involved (in wine gallons or liters, and proof).

The physical inventory will be recorded in writing as it is being taken, and retained at the place of business to which the inventory pertains for a period of at least 3 years after the filing date of the floor stocks tax return. Similarly, proprietors using a record inventory must retain that record for a period of 3 years after the filing date of the floor stocks tax return. The record of inventory must identify all products by brand name, proof, and size of container. The record must be made available at each proprietor's place of business for inspection by ATF officers. Taxpaid distilled spirits in transit as of October 1, 1985, will be included in the inventory of the person who owns the spirits as of that date.

Unmerchtable distilled spirits are not subject to the floor stocks tax. In this context, unmerchtable refers to spirits which are being returned back up the merchandising chain because of some defect. Distilled spirits which are being returned because of poor market demand or to reduce inventory are not considered unmerchtable. Although the floor stocks tax is not imposed on unmerchtable distilled spirits, all persons holding distilled spirits for sale must physically segregate any unmerchtable products and include them in a separate section of their inventory record. The unmerchtable merchandise should not be included when determining whether the dealer holds over 500 wine gallons, need not be converted to proof gallons, and should not be shown on the floor stocks tax return. If for any reason the distilled spirits are not subsequently returned or destroyed, floor stocks tax must be paid on them and the taxpayer must file an amended floor stocks return. Failure to comply with these provisions can result in the assessment of interest and penalties.

Inventory Conversion Procedures. To determine the amount of distilled spirits on hand, the inventory in liters must be first converted into wine gallons. This can be done entirely by mathematical computation using the appropriate conversion factor discussed below, or by using Chart I at the back of this Circular. (Chart I shows the amount of wine gallons in each bottle or case of distilled spirits bottled in the standard metric sizes.) Persons with more than 500 wine gallons of distilled spirits on hand (or members of a controlled group

that has a total of more than 500 wine gallons on hand) are liable for the floor stocks tax and must convert the wine gallon inventory into proof gallons.

However, persons who have determined using their own methods that they are liable for floor stocks tax may elect to convert directly from liters and proof to proof gallons. For example, a wholesaler may have several thousand cases of distilled spirits on hand. Since approximately 210 cases of 750 ml bottles would equal 500 wine gallons, the wholesaler can readily determine that his spirits will not be exempt from the tax. By using a conversion chart the intermediate step of converting to wine gallons can be eliminated.

Chart II gives factors for the conversion of standard metric sizes at the most common proofs directly to proof gallons per case; Chart III shows the factors for individual bottles. These charts are also placed at the back of this circular. Taxpayers may compute their own factors or use factors supplied by industry associations or trade journals for items bottled at proofs not shown on the attached charts. However, they are reminded that the taxpayer is responsible for the accuracy of the information shown on the tax return.

To convert the inventory to wine gallons mathematically without using a conversion chart, the quantity in liters should be multiplied by the standard conversion factor of 0.264172. (However, if the proprietor is a retailer who qualifies for the special inventory procedures discussed in the next section, a shortened factor may be used for some computations.) For each conversion by brand and size, the total wine gallons should be rounded to the nearest hundredth (for example, 75.369712 would be rounded to 75.37). There are two basic methods that can be used to convert liters to wine gallons; both will result in the same answer.

If the conversion from liters to wine gallons is made before multiplying the total number of cases or bottles to be converted, then the result should first be rounded to the nearest sixth decimal place. Then multiply that figure by the total number of units to determine the wine gallon amount. This final answer should be rounded off to the nearest second decimal place (that is, to the nearest hundredth of a wine gallon). For example, if you had seven 1.75 Liter bottles on hand, you could convert a single bottle to its wine gallon equivalent using the factor, carry out the answer to the sixth decimal place, multiply by seven, and round that answer off to the nearest second decimal place to get the final wine gallon figure.

Alternatively, the conversion from liters can be made after computing the total number of liters in the cases or bottles. This answer can be rounded directly to the nearest second decimal place. Using the figures from the example above, the 12.25 Liters in those bottles (1.75×7) can be multiplied by the factor and the answer rounded to two decimal places. Both methods result in the same answer of 3.24 wine gallons.

To determine the proof gallon amount, multiply the number of wine gallons times the proof of the product, divide by 100, and round the answer off to the nearest first decimal place (that is, to the nearest tenth of a proof gallon). If the seven bottles discussed above were 80 proof, their proof gallon content would be 2.6 (3.24×80 divided by 100 = 2.592, rounded to 2.6 proof gallons). Remember, the wine gallon quantity must be rounded to the nearest second decimal place (to the nearest hundredth of a proof gallon), and the proof gallon quantity must be rounded to the nearest first decimal place (to the nearest tenth of a proof gallon).

There is one other method that may be used to inventory full cases of distilled spirits only. Many cases will have the wine gallon content marked on the side of the case; some cases will have the proof gallon content also marked. Whenever these markings are found, proprietors may use them in lieu of any other conversion method.

The following examples illustrate the various conversion procedures:

Example 1: Using Chart I, determine whether the following inventory falls within the 500 wine gallon exemption:

45 cases of 750 ml. bottles	-	45 X 2.377548	=	106.99
32 cases of Liter bottles	-	32 X 3.170064	=	101.44
40 cases of 500 ml. bottles	-	40 X 3.170064	=	126.80
17 cases of 1.75 L. bottles	-	17 X 2.773806	=	47.15
Total wine gallons in inventory				382.38

Example 2: Using Chart II, convert the following inventory items to proof gallons:

# cases	size	brand name	proof	conversion	proof gallons
110	750 ml	XX bourbon	80	110 X 1.902038	209.2
250	1.75 L	YY schnapps	60	250 X 1.664284	416.1

Example 3: Without using a conversion chart, convert 10 cases of 750 milliliter bottles of 80 proof bourbon to wine gallons and then to proof gallons (each case contains 12 bottles).

12 bottles X .75 liters = 9.00 liters per case;
9.00 liters X 10 cases = 90.00 total liters;
90.00 liters X 0.264172 = 23.77548 wine gallons;
23.78 wine gallons X .8 (80 proof ÷ 100) = 19.024,
rounded to 19.0 proof gallons.

or

one 750 ml bottle = .750 Liters;
.750 X 0.264172 = 0.198129 wine gallons per bottle;
0.198129 X 120 bottles = 23.77548 rounded to 23.78;
23.78 wine gallons X .8 = 19.024, rounded to 19.0 proof
gallons.

Special Inventory Procedures. Retailers of distilled spirits must use the above inventory procedures for computing the quantity of full cases on hand. However, retailers may use the following special procedures for taking a physical inventory of open stock (products in less than full cases):

1. The record of inventory may list the total number of bottles by size and proof only.
2. Fractional label proofs may be rounded to the nearest whole proof (for example, 86.8 proof would be rounded to 87 proof).
3. A shortened conversion factor of 0.26 may be used for converting quantities in liters to wine gallons.
4. The quantity of spirits in all open bottles of the same proof, regardless of size, may be totalled and shown as one entry (for example, "Miscellaneous bottles, _____ proof = _____ Liters).

Retailers who choose to round fractional proofs and use the shortened conversion factor must use both of these special procedures consistently throughout their open stock inventories.

The following example illustrates the use of these special inventory procedures:

Convert 25 750 milliliter bottles of 86.8 proof spirits to wine gallons, and then to proof gallons.
25 bottles X .75 liters = 18.75 liters
18.75 liters X 0.26 = 4.875 wine gallons, rounded to 4.88
4.88 wine gallons X .87 proof = 4.2456 proof gallons
After rounding, the total would be 4.2 proof gallons.

Computing Tax Liability. The total tax liability, before taking any credit, is determined by multiplying the total proof gallons in inventory times \$2.00. For example, 870.2 proof

gallons X \$2.00 = \$1740.40. The \$800 credit is then subtracted from the computed tax to determine the total tax due. Remember, the credit may not exceed to computed tax; therefore, if the computed tax is \$570.40, a credit of \$570.40 would be taken on the tax return, and the tax due would be \$0. Also, members of controlled groups are reminded that the controlled group is entitled to a single credit, which may be apportioned among the members in any manner satisfactory to them.

Paying Floor Stocks Tax. All persons holding distilled spirits for sale on October 1, 1985, must file a tax return. Persons with 500 wine gallons or less in inventory, and those who have no tax liability as a result of the credit are not exempt from filing a tax return.

The floor stocks tax return (IRS Form 11) will be distributed to proprietors by September 15, 1985. Additional forms may be obtained from IRS and ATF offices.

The floor stocks tax return must be filed with the appropriate Internal Revenue Service Center, with full payment, on or before April 1, 1986. However, small and medium-sized dealers may elect to pay the tax in three equal installments due on or before April 1, July 1, and October 1, 1986. To qualify for installment payments, controlled groups must apply the \$500,000 gross sales receipts criteria to the group as a whole. The Internal Revenue Service will bill these dealers for the installment payments due on or before July 1, and October 1, 1986. These dealers will be responsible for filing the tax return with the first payment on or before April 1, 1986.

CHART I - CONVERSION OF LITERS TO WINE GALLONS

<u>Bottle size</u>	<u>Bottles/case</u>	<u>W.G./bottle</u>	<u>W.G./case</u>
50 mL	120	.013209	1.585032
100 mL	60	.026417	1.585032
200 mL	48	.052834	2.536051
375 mL	24	.099065	2.377548
500 mL	24	.132086	3.170064
750 mL	12	.198129	2.377548
1 Liter	12	.264172	3.170064
1.75 L	6	.462301	2.773806

CHART II - PROOF GALLONS PER CASE

Proof	100mL & 50mL	200mL	750mL & 375mL	Liter & 500mL	1.75L
25	.396258	.634013	.594387	.792516	.693452
30	.475510	.760815	.713264	.951019	.832142
35	.554761	.887618	.832142	1.109522	.970832
42	.665713	1.065141	.998570	1.331427	1.164999
48	.760815	1.217304	1.141223	1.521631	1.331427
54	.855917	1.369468	1.283876	1.711835	1.497855
56	.887618	1.420189	1.331427	1.775236	1.553331
60	.951019	1.521631	1.426529	1.902038	1.664284
70	1.109522	1.775236	1.664284	2.219045	1.941664
75	1.188774	1.902038	1.783161	2.377548	2.080355
78	1.236325	1.978120	1.854487	2.472650	2.163569
80	1.268026	2.028841	1.902038	2.536051	2.219045
86	1.363128	2.181004	2.044691	2.726255	2.385473
86.8	1.375808	2.201292	2.063712	2.751616	2.407664
90	1.426529	2.282446	2.139793	2.853058	2.496425
90.4	1.432869	2.292590	2.149303	2.865738	2.507521
94.4	1.496270	2.394032	2.244405	2.992540	2.618473
100	1.585032	2.536051	2.377548	3.170064	2.773806
101	1.600882	2.561411	2.401323	3.201765	2.801544
190	3.011561	4.818497	4.517341	6.023122	5.270231

To use this chart: total the number of cases (by brand) of each size and proof, multiply by the factor in the appropriate column, and round the result to the nearest first decimal place (i.e., to the nearest tenth of a proof gallon).

CHART III - PROOF GALLONS PER BOTTLE

Proof	50mL	100mL	200mL	375mL	500mL	750mL	1L	1.75L
25	.003302	.006604	.013209	.024766	.033022	.049532	.066043	.115575
30	.003963	.007925	.015850	.029719	.039626	.059439	.079252	.138690
35	.004623	.009246	.018492	.034672	.046230	.069345	.092460	.161805
42	.005548	.011095	.022190	.041607	.055476	.083214	.110952	.194166
48	.006340	.012680	.025360	.047551	.063401	.095102	.126803	.221904
54	.007133	.014265	.028530	.053495	.071326	.106990	.142653	.249643
56	.007397	.014794	.029587	.055476	.073968	.110952	.147936	.258889
60	.007925	.015850	.031700	.059438	.079252	.118877	.158503	.277381
70	.009246	.018492	.036984	.069345	.092460	.138690	.184920	.323611
75	.009907	.019813	.039626	.074298	.099065	.148597	.198129	.346726
78	.010303	.020605	.041211	.077270	.103027	.154541	.206054	.360595
80	.010567	.021134	.042267	.079251	.105669	.158503	.211338	.369841
86	.011360	.022719	.045437	.085195	.113594	.170391	.227188	.397579
86.8	.011465	.022930	.045860	.085988	.114651	.171976	.229301	.401277
90	.011888	.023775	.047551	.089158	.118877	.178316	.237755	.416071
90.4	.011941	.023881	.047762	.089554	.119406	.179109	.238811	.417920
94.4	.012469	.024938	.049875	.093516	.124689	.187034	.249378	.436412
100	.013209	.026417	.052834	.099065	.132086	.198129	.264172	.462301
101	.013341	.026681	.053362	.100055	.133407	.200110	.266814	.466924
190	.025096	.050192	.100385	.188222	.250963	.376445	.501927	.878372

To use this chart: total the number of bottles (opened cases) of each size and proof, multiply by the factor in the appropriate column, and round the result to the nearest first decimal place (i.e., to the nearest tenth of a proof gallon).

Inquiries. Please direct any inquiries concerning the floor stocks tax to the appropriate floor stocks tax coordinator in the nearest ATF regional office, listed below:

Midwest Region

Bureau of Alcohol, Tobacco
and Firearms
230 S. Dearborn St.
15th Floor
Chicago, IL 60604
(312) 886-5149

Bureau of Alcohol, Tobacco
and Firearms
500 Main Street, Rm. 6510A
Federal Office Bldg.
Cincinnati, OH 45202
(513) 684-3334

North Atlantic Region

Bureau of Alcohol, Tobacco
and Firearms
6th Floor
6 World Trade Center
New York, NY 10048
(212) 264-3994

Bureau of Alcohol, Tobacco
and Firearms
Fed. Bldg./U.S. P.O.
Sixth Floor
Ninth & Market Streets
Philadelphia, PA 19107
(215) 597-3984

Southwest Region

Bureau of Alcohol, Tobacco
and Firearms
1114 Commerce Street
Room 701
Dallas, TX 75242
(214) 767-2257

Southeast Region

Bureau of Alcohol, Tobacco
and Firearms
3835 Northeast Exwy.
Room 200
Atlanta, GA 30340
(404) 455-2645

Western Region

Bureau of Alcohol, Tobacco and Firearms
525 Market Street
34th Floor
San Francisco, CA 94105
(415) 974-9620

Director

McCarron;3/22/85
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CODE	INITIATOR	REVIEWER	REVIEWER	REVIEWER	REVIEWER	REVIEWER	REVIEWER
SUR-NAME	McCarver	Hardy	Graham	Moad	R. Gaudin	Daniel	Black
DATE	6-26-85	6-26-85	6-27-85	6-28-85	7/8/85	7/8	7/10

ATF F 1325.6 (2-75) CORRESPONDENCE APPROVAL AND CLEARANCE

REPLACES ATF FORM 92 (9-73) WHICH MAY BE USED

DEPARTMENT OF THE TREASURY
BUREAU OF ALCOHOL, TOBACCO AND FIREARMS